Exhibit D

UNITED STATES BANKRUPTCY COURT

SOUTHERN DISTRICT OF NEW YORK

Case No. 08-01420-(JMP)(SIPA)

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In the Matter of:

LEHMAN BROTHERS INC.,

Debtor.

- x

U.S. Bankruptcy Court

One Bowling Green

New York, New York

January 8, 2014

10:02 AM

B E F O R E :

HON JAMES M. PECK

U.S. BANKRUPTCY JUDGE

Hearing re: Trustee's Motion for an Order (1) Confirming the Trustees Denial of SIPA Customer Status to Claren Road Credit Master Fund Ltd. and (2) Subordinating the Claim [LBI ECF No. 7539]

Hearing re: Trustee's One Hundred Fourth Omnibus Objection to General Creditor Claims (No Liability Claims)[LBI ECF No. 6768]

Transcribed by: Dawn South

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P R O C E E D I N G S

THE COURT: Be seated. Good morning.

(A chorus of good morning)

THE COURT: Please proceed.

MR. SALZMAN: Thank you, Your Honor. Good morning, I'm Michael Salzman from Hughes Hubbard & Reed, the attorneys for the SIPA Trustee in the LBI case.

This morning we have two motions on. I -- with the Court's permission I intend to argue the Claren Road motion, and my colleague, Mr. Funkhouser, will be arguing the one hundred and fourth omnibus motion, the one concerning the underwriters. Both motions have in common a legal issue but there are factual differences, and in our view, subject to whatever Your Honor might think, we think it'd be more orderly just to take the motions one at a time.

THE COURT: That's fine.

MR. BAREFOOT: Your Honor, if we may briefly be heard on just the order of argument?

THE COURT: Okay. I did say that's fine, but didn't mean to preclude somebody saying it's not fine.

MR. BAREFOOT: Just as a background, the reason we --

THE COURT: You want to say who you are for the record and who you represent?

MR. BAREFOOT: My apologizes, Your Honor. Luke

Barefoot from Cleary Gottlieb for the junior underwriter claimants.

And the reason that we had consolidated these two proceedings was so that the common legal issue of 510(b) could be argued together and decided together.

So our proposal was that, of course Mr. Salzman could proceed with the argument of 510(b), and then we had divided the labor among the -- the various claimants on the 510(b) issue.

There are certainly independent and different arguments for the junior underwriters in terms of subordination and no liability, but given that we've already consolidated these so that they could be heard together, I'm afraid it would be overly repetitious or moot to have Claren Road entirely argued before reaching any portion of the junior underwriters' arguments.

THE COURT: Well, I'm not going to quibble with you over the use of the term consolidated. They're being heard at the same time. And when we had a telephone conference regarding scheduling it was clear to me that there were common legal issues that affected both of these contested matters, but that did not necessarily mean that they were one in the same. Indeed Claren Road made a strenuous argument that I summarily rejected by the way that it should be heard separately.

So I don't really care what the order of play turns out to be here, because the differences will need to be highlighted and the similarities will need to be highlighted, and the only issue efficiency of presentation.

I'm mindful of your comment, but I think it is ultimately cleaner for these to be heard as independent matters that have certain common issues and certain distinguishing factors, and if it's repetitious that's my problem, not yours.

MR. BAREFOOT: Very good, Your Honor. Thank you.

MR. SALZMAN: If I may proceed, Your Honor.

This is the trustee's motion for mandatory subordination of a claim by bondholder of bonds issued by LBI's parent, Lehman Brothers Holdings.

Claren Road filed a claim against LBI because LBI failed to complete a purchase of LBHI bonds during Lehman week. It was the Friday before Lehman week that the transaction was initiated, and it was supposed to settle on Wednesday of Lehman week, and it didn't settle and eventually Claren Road made a claim against LBI because the bonds declined in price during -- during Lehman week.

Section 510(b) is the mandatory subordination provision. It says:

"That a claim for damages arising from the purchase or sale of a security of the debtor or an affiliate

of the debtor, quote, 'shall be subordinated' to all claims or interests that are senior to or equal the claim or interest represented by such security."

We submit that's exactly what we have here. We have a claim for damages. The claim arises from an aborted sale and it's a sale of a security without any doubt, and it's equally without any doubt security of an affiliate of the debtor.

So on this motion we think there's no factual dispute and the Court can rule based on the papers submitted.

Claren held bonds issued by LBHI, two issues of Euro denominated senior notes, Claren tried to sell them to Lehman on the Friday before Lehman week, LBI failed to complete the trade, and Claren's claim is stated as a damages claim for the loss and value of the bonds between the trade date, that Friday before Lehman week, and the SIPA filing date, the following Friday.

Claren also made a claim for the full principal amount of the bonds in the LBHI case, and those are claims number 64113 and 64114 in the LBHI case. And we've submitted them in the Hoffer declaration in reply.

It's also a record fact that holders of those bonds have recognized interest under the LBHI reorganization plan. Those ISIN numbers are specifically and expressly

recognized in the LBHI case.

On these facts we submit, Your Honor, the words of the statute are sufficient to provide the result.

THE COURT: Let's -- I hear that, and this is an interesting presentation of a 510(b) issue. It is really not plain vanilla, although I know you're presenting it as plain vanilla. And one of the things that I have been thinking about, as I prepared for the hearing, is the problem in 510(b) that is created by the reference to securities of an affiliate of the debtor and the lack of obvious symmetry between the words of the statute in reference to, quote, "shall be subordinated to all claims or interests that are senior to or equal the claim or interest" -- and here are the words I'm emphasizing, "represented by such security." I think everybody is dancing around these words.

The cases are uniform in agreeing with you. The problem that I'm having, as I think about this, is that the happenstance that the trade involved an affiliate of the debtor, LBHI, is what triggers the 510(b) subordination, but the conduct in question, namely the execution of a trade, is the ordinary course conduct of LBI as a functioning broker/dealer.

So one of the questions that I have, and I'd like you to address this, is why, other than the fact that the

statute says what it says, and I'm not disregarding that, but why does it make sense for there to be a different outcome in a failed trade with respect to LBHI bonds and any other corporate bond that might have been the subject of a failed trade during Lehman week? That's the heart of my concern.

MR. SALZMAN: I'm happy to address that and I had prepared to address that.

Our adversary did talk in its paper about how this could, for example, have been Apple ink bonds rather than Lehman bonds.

THE COURT: And that was not chosen randomly, it was because Judge Walrath --

MR. SALZMAN: Right.

THE COURT: -- happened to use that example in the WAMU case.

MR. SALZMAN: Right. Understood. And let me go directly to that.

There may be some other case out there where it is ordinary course of business and it may have been happenstance that they were bonds of the affiliate. This is not that case. And it's most clearly not that case if you look as we stated in our reply paper at what LB -- sorry -- what Claren Road put in its original claim in the LBHI case. They made a claim there with respect to the same damages,

the same loss and value during Lehman week, and in that paper, which it filed months -- September -- months after Lehman week -- September of 2009 and claiming against LBHI it said, we have a claim for damages against LBHI or some affiliate of LBHI upon information and belief it was somebody in the Lehman family, is the effect of what they were saying.

So from the point of view of Claren Road it was not the bad luck. It could have called Merrill to execute the trade, it could have called Morgan Stanley to execute the trade, and just its bad luck it called Lehman to execute that trade. That's not what happened, apparently.

What the record shows is that it called someone at Lehman after the parent -- the day -- I guess the day before that parent was going to -- the business day before that entity was going to file for bankruptcy and said in substance, please take back these bonds, and the person at -- the way that worked Lehman would have been through the broker, but it was really about Lehman and getting out of Lehman and calling Lehman to get out of Lehman.

And so this case is not a case where it's ordinary course of business. The --

THE COURT: Well you raise a question that I'm not sure is directly part of what I was addressing, but let me respond to it.

I recognize that there is in this rather clean legal assessment of 510(b) context that is not clean, and you are adverting to that both in your reply papers where you make reference to not the unclean hands of the claimant, but the claimant acting almost desperately to try to extricate itself from its investment that is going down the tube literally within days.

And it's also clear to me from the papers I have looked at that Claren Road is a prime brokerage customer of Lehman Brothers in its broadest and least specifically tethered to legal entity term because of the relationship with LBIE, the fact that it was making claims that ultimately were disallowed as part of the settlement with LBIE.

And I recognize that there is more going on here in terms of background than the somewhat surgical analysis that we're looking at today of some fairly opaque language in 510(b), but my question to you was actually a much simpler one.

Assume for the sake of discussion that the trade in question is a trade that involves a bond issued by Morgan Stanley, to use your Morgan Stanley example. They're not executing the trade, it just happens to be a bond of theirs. Why should it make a difference to the trustee and the trustee's constituent of unsecured creditors that the bond

in question is of an affiliate or of a non-affiliate? Because the conduct in question is simply the failure to close the trade.

MR. SALZMAN: The classic case under 510(b), and this goes back well before 510(b) itself existed, was the concern that debt would turn into equity, that people had -- sorry -- equity would try to turn into debt, that people near the bottom of the priority chain would try to move up. That's -- and 510(b) -- the core of 510(b) is about upholding the absolute priority rule.

THE COURT: By the way, never before today did I think that a 1973 law review article by Slane (ph) and Kripke from the NYU law review would take on such significance. And I'm just going to let everybody know, I don't think it's that significant.

So that the fact that we're going to be talking about legislative history that may have been influenced by a law review article is in my view absolutely meaningless to my analysis here today. This is a plain language decision.

I've read the Del Biaggio case, not to be confused with Major Deblasio, and I know Judge Carlson (ph) and I think it's a good opinion, and I highlighted for myself what he wrote on page 5 of my copy of the opinion, which is a Westlaw cite. Quote, "This Court must apply the plain language of section 510(b) even if that language goes beyond

the stated policy rationale for the statute." And it cites to RadLAX.

And just so everybody is clear on this, Homer Kripke was a professor of mine at NYU Law School. He's a -- he's a great guy -- or was. He has nothing to do with today's decision. This decision is going to be made purely on the basis of applying the words as written to the facts presented.

MR. SALZMAN: Let me explain.

First a footnote in the form of an apology, or an apology in the form of a footnote, which is that last night it came to my attention -- our attention, that the Del Biaggio case was affirmed by the District Court in November, and I apologize for not having put that in the brief. We've handed copies to our adversary, and I'm happy to hand one up for the Court's convenience if you'd like me to do that.

THE COURT: That's fine, it's not going to -- I might want to have it to the extent I write something here, but it's not going affect today's argument.

MR. SALZMAN: And -- thank you, Your Honor.

Let me get directly to why application of the plain words makes sense in this case.

This is not a case of equity trying to become debt, but it is a case of debt in one case trying to become debt in two cases.

They have a good claim in the LBHI bankruptcy for the value of the bonds as they turned out to be at the end of -- by -- as of the -- as of the filing date of that case. There's a plan, those bonds are going to be paid, whatever is in the till for them from the reorganization plan and those bonds have been recognized by this Court. The interest in those bonds have been recognized and a distribution is being made accordingly.

Here these folks are also seeking to get onto a second chain of priority, and the affiliate clause, one of its affects, is to say, no, you can't get onto two different chains of priority in a corporate family, it's -- and there are good policy reasons for that.

The financial structure of LBI was intimately tied in with the financial structure of LBHI, LBHI funded LBI every day, when LBI had excess cash it went to LBHI, the capital for LBI came from bonds that the parent would offer to the public.

And so the congressional judgment, we submit, makes sense certainly in this case, I'm not going to say in every conceivable case, I don't have to do that, that a bondholder of the parent has rights against the parent, but it's not supposed to dilute the claims of ordinary creditors of a subsidiary and get two bites at the apple.

The classic case, the debt turning into -- equity

turning into debt is an example of somebody attempting to get a bigger bite at the apple.

This case, it's an instance of a creditor trying to get two bites at the apple, and the affiliate clause says you can't do that, at least not until the real creditors of the subsidiary are paid in full.

THE COURT: What are the claims or interests that are represented by the LBHI bond?

MR. SALZMAN: Well they are nul interest. They say I want money from you, the subsidiary, and the answer is, you're on the wrong line, sorry, get over on that line. And that's what the Del Biaggio case, the VF Brands case, and the Learnoud (ph) case talk about, that they're separate lines, and sorry, you're on the wrong line, and therefore you go to the bottom or the back of the line.

THE COURT: I understand -- I understand the cases that have considered this conundrum, and what I'm struggling with isn't the legislative history, but simply scanning the text. And so if you scan the text and you get into this actionable section everybody I think will concede that there is a triggering of potential 510(b) subordination by virtue of the framing of the issue. We have the failed trade of a security of an affiliate of the debtor. We're ready to subordinate it.

Now how do you do that when it's being

subordinated to all claims or interests that are senior to or equal the claim or interest, bolded language, represented by such security? The security in question is the security of an affiliate of the debtor, its parent, and there are no claims or interests in the LBI case that are represented by that security, are there?

MR. SALZMAN: Well, I would say there are no valid interests. It's like a zero interest, and it's saying -- in this case, which is an extreme case, you're at the end, you're at the very end, you're below zero, you -- anyone would be senior to you, and that's how the Del Biaggio case and the other cases I mentioned deal with that, and they don't -- they don't -- I understand the issue, but in this case it's you get -- you go last because the security -- your security, these bonds, you -- it's subordinated to zero. Your interest in this estate is nothing and you get subordinated to everyone. Equal to. It doesn't have to be senior to, it can be equal to the claim.

THE COURT: Well see here's what I think, and this is why we're struggling with this, or I recognize I'm the one who's forcing the question, but I think what happened when they added the language to include or an affiliate of the debtor is that those drafting the language didn't fully think about how that really works when you're dealing with a claim or interest represented by that security of the

affiliate. Because the security of the affiliate really isn't a claim in the debtor's case is it?

MR. SALZMAN: It's not a good claim.

THE COURT: What?

MR. SALZMAN: It's not a good claim.

THE COURT: Well is it -- why is it -- let's think about that.

In what respect does the holder of LBHI bonds in a case that is not substantively consolidated have any standing at all in the LBI case?

And I reference some hearings that you did not attend that occurred within the last month where counsel for LBHI, in the context of a hearing to disallow the claims of certain employees of LBI, argued that by virtue of a settlement between LBI and LBHI, by virtue of the separate confirmed plan for LBHI, and by virtue of the separate administration of the SIPA case for LBI, LBI former employees had no standing to assert alter ego type claims against LBHI. I entered orders consistent with that.

So we're not dealing with consolidated estates, we're dealing with demonstrably separate estate administrations. And while substantive consolidation might at one time have been an acted issue, it's now finally settled by virtue of the confirmed plan and by virtue of the settlements and by virtue of the law of the case.

So in this setting, thinking about LBHI bonds, what claims are represented by that security in the LBI case?

MR. SALZMAN: I guess as a -- one answer at least is that as an economic matter if we had a situation where LBI was -- had -- it turned out could pay everybody then among the people it could pay would be its parent stockholder, and indirectly, as an economic matter, holders of bonds of LBHI would -- would benefit from that.

THE COURT: That might --

MR. SALZMAN: That's an economic matter, that's not a legal matter, and I --

THE COURT: But that could only occur on some other planet in our galaxy, not here.

MR. SALZMAN: Fair enough. Well that's not the Lehman case. I understand that's not the Lehman case, but obviously a statute is written for all purposes and for, you know --

THE COURT: Can you actually envision a situation in which there is a debtor enterprise which is so solvent that it pays off not only all of its creditors but all of the creditors of its parent? I mean it's hard to imagine frankly, but I'll accept that it's a hypothetical that might pass in a first year law school class.

MR. SALZMAN: Fair enough.

The -- the legal -- the more direct legal answer is that I submit that as found in those other cases that the -- most courts were comfortable with Del Biaggio, in particular, with the proposition that it's not a good -- it's not at a good claim, it's a zero claim, but that's what makes sense to make sure that a bondholder of an affiliate of an equity holder of an affiliate doesn't get two bites at the apple.

THE COURT: Would you acknowledge that the words do not scan all that well?

MR. SALZMAN: I acknowledge that you could have written a statute that was three times longer that dealt with affiliates in more detail, yes.

THE COURT: All right. Anyway, I've been interrupting you, go ahead with your argument.

MR. SALZMAN: No, that's fine.

I think we -- Your Honor's questions really got to the heart of the matter, and I don't want to belabor it, but I would go back to the proposition that there's no doubt that the bond -- the bonds are securities, our opponent attempts to make some argument that bonds shouldn't even be part of the statute. Clearly they are and there are plenty of cases that enforce the statute as to bonds.

Likewise the affiliate clause is really in the statute. Claren Road makes some effort to say well maybe

that was just a mistake and it points to a different law review article that speculates that a better statute wouldn't have talked about affiliates at all, but that's not the law.

And -- and on policy grounds I think you do get to the right result if you don't allow Claren Road to get a full claim like every other bondholder in the LBHI case and also a claim for the fallen value of those bonds during -- during Lehman week.

In effect those bonds fell in value during that week, precisely because the prospect that in the bankruptcy, which had already begun, bondholders were not going to be paid in full, and that's what that trading was all about. And for Claren Road to get what bondholders in that case get and also get the declining value during that week is a form of double recovery. It's not -- I'm not saying they're getting more than 100 percent, but it is a form of double recovery.

There's the value of the bonds, that's what they get, and then there's also -- but we also get the decline in value during that week is we submit double recovery, not fair to the creditors of LBI, and so you do get to the right result by subordinating.

THE COURT: I hear your argument, but I'm going to interpose maybe a different perspective, which goes back to

the failed trade of Apple shares of that earlier hypothetical.

Isn't the claim not a double recovery claim as much as it is a claim for the failure to complete the trade, which is of course what LBI as a broker/dealer undertook to do? So it's a breach claim.

MR. SALZMAN: But the measure of the damage as it turns out -- or not as it turns out -- necessarily so, the measure of the damage they allege is precisely people thinking through -- the market thinking through this is a bankruptcy, this is a bad situation, you don't want to be in these bonds, and so the price is going down to people's guess as to what's going to happen in that bankruptcy. The bankruptcy had already occurred by the -- by the settlement date, not by the trade date.

But so on the Friday before the rumors were there, the news was there, people who knew understood that the bankers were meeting to figure what to do about Lehman Brothers, and if hypothetically all the holders of those bonds had called LBI and said I want out, sell all my Lehman bonds on that Friday, you could work through that situation, and you would have aggregated the double recovery problem that I talked about before.

THE COURT: Okay. So to sum up it's your position that the issue having been framed, the language of 510(b),

when applied here, leads to an almost no-brainer that the claims of Claren Road should be subordinated.

MR. SALZMAN: Yes, and beyond the words, this Court is not supposed to do anything in a robotic fashion, it's supposed to apply the words as it can and not lead to an absurd result, and we've explained I think why far from an absurd result it's the correct economic result, it's the correct result consistent with the purpose of the statute, and for that reason we ask that Your Honor grant our motion.

THE COURT: Okay. Thank you.

MR. SALZMAN: Thank you.

MR. KING: Good morning, Your Honor, Marshall King from Gibson, Dunn & Crutcher on behalf of Claren Road.

Your Honor has put your finger on most of the reasons I think why this isn't a plain vanilla application of the plain words of the statute. Let me see if I can add one or two that weren't discussed with counsel for the trustee and put it in a legal framework and a context that explains why because of the issues Your Honor has identified and the difficulty in applying the plain words, why it means we win here and that subordination is not appropriate.

You and counsel for the trustee went through pretty extensively the ambiguities in trying to figure out to what do we subordinate this claim? And the cases -- and by my count there are about three cases that find in favor

of the trustee's position in this type circumstance, but they really all go back to Judge Walrath in VF Brands.

The Del Biaggio, for instance, both in the District Court -- the Bankruptcy Court and the District Court, which I saw, you know, for ten minutes before we started this morning, relied on VF Brands --

THE COURT: Uh-huh.

MR. KING: -- the Judge Walrath case. And you know, truthful she just got it wrong in that case honestly. I really think it is -- she misinterpreted the statute. She read it as saying the claim or interest represented by the claim filed by the claimant as opposed to the claim represented by the security. She sort of -- and that becomes somewhat circular in that context, because someone has asserted a general unsecured creditor claim she then treated the subordination as being subordinated to general creditors.

But what Your Honor has rightly pointed out is you have to look at what claim does the security represent? And in this context there's nothing. There's nothing to subordinate it to. And the idea that -- and previously the trustee took no position. In its papers there was no explanation of to what should this be subordinated, to what level should it go? They sort of just said, well, whatever it is it's below general creditors and that's good enough

for here. But today Your Honor dragged it out of him, he thinks it's below nothing, below zero essentially. And there's really no logic to subordinating this ordinary course contractual obligation that LBI undertook to zero -- to less than zero. I'm sorry, it's not even zero, it's less than zero, which is what he's advocating here. There's no good reason to treat it that way. And the -- the plain words of the statute don't require that.

The plain words of the statute are ambiguous in this circumstance, because you don't have a claim in the priority structure of the debtor, who we're dealing with.

THE COURT: Well couldn't you, just to be a creative thinker here, couldn't you conclude that the only way to make logical sense out of this is that there's a virtual security, in effect if the security of the affiliate were a security of the debtor then the claim represented by such security would be an unsecured claim, and so you would then subordinate to that hypothetical security.

How else could you make sense of this other than by assuming that in the case of an affiliate, because you have separate chains, that the claim represented by such security in the bankruptcy case either assumes consolidation or assumes that it would be somewhere in the capital stack of the debtor as if it were a like type security?

MR. KING: That's -- that's in substance what the

-- if I recall the Learnoud case concluded. Although in Learnoud I should point out the reason I said it all boils down to VF Brands, in Learnoud the parties actually didn't dispute that it needed to be subordinated to general unsecured creditors, and so the issue wasn't really joined on the issue that we have here today. But could you do that? You could do that, but certainly the plain words of the statute don't dictate that.

There are multiple interpretations of this statute, and that's exactly what the Second Circuit has held, means that this is ambiguous, and one then needs to look at the legislative history and the policies underlying this statute.

And perhaps there are circumstances, perhaps even the Del Biaggio case as a decent example there's a policy reason for saying yes subordination here where the parent -- or the parent -- the debtor parent essentially used the subsidiary as part of the fraud and it was one -- one big inextricable scheme in -- and it's not unusual for a party to use a subsidiary in fraud -- and in such circumstances you could say yes, the policies underlying the statute that a -- that someone -- and someone deciding to invest getting the expectations of a shareholder shouldn't be able to elevate his or her claim to that of an ordinary creditor -- a debtor -- of a debtor.

But it's precisely when you look at the policies underlying the statute that Claren Road's claim should not be subordinated.

There is not a single argument to be made that subordinating this claim for either of the two policy objectives.

And I'm going to defend Slane and Kripke for a moment if you allow me. Not because Slane and Kripke aren't smart guys and --

THE COURT: But they are.

MR. KING: -- but not because of that, because the Second Circuit says those are the policies. Regardless of -- it's not because there was a great intellectual law review article, it's because that law review article is what led congress to enact the statute, and the Second Circuit says in cases of ambiguity the only time we're going to subordinate is if one of those two policy rationales is furthered by that subordination. And those two policy rationales are taking on the risk and return expectations of a shareholder rather than a creditor, and where the claimant seeking to recover a contribution to the equity pool that's presumably been relied on by other creditors of the debtor.

Trustee -- nobody argues that that's -- that those policies are furthered by Claren Road. Claren Road is obviously not trying to elevate itself from a shareholder

and cloak itself in the garb of a creditor. And there's no argument to be made that any creditor of LBI relied on any equity contribution that was somewhere buried in this chain of events.

Before I even get to that I did want to point out there's another reason why there's ambiguity here in this statute, and it's something that both Your Honor and counsel for the trustee mentioned.

The statute by its literal terms applies to damages arising from the purchase or sale of a security.

Here, as the trustee's counsel put it, we have an aborted sale, and Your Honor called it a failed sale.

The statute by its literal terms applies to an actual purchase or sale. Here we don't have that. We have the absence of one.

Now, I concede that the cases, such as Med Diversified in the Second Circuit, once they find -- find ambiguity in those circumstances and then opine the policy rationale usually find that that -- the statute applies to such cases, that it -- that even though it was a failed consummation of a stock purchase, for instance, the claim nevertheless arises from the purchase or sale of security. So in other words, the statute can apply to a failed sale. But again, only when those policies -- one of those two policy rationales is furthered. And this is not one of

those situations. We have in fact the opposite, the flip side if you will of Med Diversified.

Claren Road wasn't looking to invest in Lehman, Lehman broadly speaking, Claren Road was looking to get out of Lehman. It was a -- it was a transaction separate from the decision to invest and to become a bondholder of the parent. And therefore its expectations -- in Med Diversified the Court said, well this employee who was supposed to get stock, he had the expectations of a stockholder, he had the expectations of unlimited upside, and he should be bound to that, he shouldn't get the best of both worlds.

We have the opposite. We capped our recovery here at the purchase price. We had -- once -- once the contract was entered into that was then breached we had an upside capped in a fixed amount. There's no -- that's not an investment speculation that we were engaged in, we were trying -- we'd fixed the price and we're not being treated as an investor. And so it's really the flip side of Med Diversified where the policies definitely don't apply.

I want to address the dual recovery issue that was -- that was mentioned and how Mr. Salzman tried to justify subordination under the policies. He sort of -- he said you -- one of the policies, although it's not mentioned by the Second Circuit in Med Diversified when it said the only --

when it identified the only two policies -- was simply that -- was to not allow debt in one case to try to become debt in another case. Respectfully, that doesn't distinguish our case from the Apple bond or the Morgan Stanley bond.

We had two separate independent obligations by two separate independent obligors. We made an investment in LBHI and had the bonds and thus became a creditor of LBHI, but separately -- a separate transaction we tried to -- we had a contract with LBI and tried to settle that, and they breached that separate obligation.

The -- that's not dual -- the fact that we made a claim -- by the way we have since sold the claim so it's not like we're getting a dual recovery as a matter of fact, but we aren't getting into the facts here too much --

THE COURT: Then I will completely disregard the fact that you sold your claim.

MR. KING: Well, I'm not asking you to disregard the fact that we sold the claim, but they're making an argument that we're getting a dual recovery, and my point is simply that isn't the fact.

THE COURT: Well whether you sold the claim or not it shouldn't affect the legal analysis today.

MR. KING: It absolutely should not, and therefore the issue of a dual recovery shouldn't affect the analysis -- the potential dual recovery shouldn't affect the

analysis.

But --

THE COURT: Are you suggesting that there is a potential characterization of this as dual recovery? Because even in my discussion with trustee's counsel I distinguished the two.

MR. KING: I distinguished the two as well, Your Honor. I --

THE COURT: For the same reasons or for different reasons?

MR. KING: I think that's a total red herring. The question is the claim against LBI arises out of an independent obligation by LBI.

And the point I guess I was trying to lead to by a roundabout route was had we bought a Morgan Stanley bond and the same facts then occurred as occurred here we'd have a right -- we'd still have the Morgan Stanley bond -- we'd have a right to collect from Morgan Stanley, we'd also have a right in damages against LBI for breeching its obligation to purchase it at -- at a sum certain.

And while there may be issues down the road of whether we could or could not acquire -- I'm sorry -- recover more than 100 cents on the dollar, that scenario is not happening in our circumstance.

And so the idea that you can't have two parties

obligated for two separate independent obligations that somehow relate to, you know, a similar body of facts, is just wrong. That -- that doesn't -- that is not the policy underlying this statute. And the affiliate issue doesn't -- doesn't change that. There really is no justification in this circumstance.

You could have circumstances where an affiliate -- the debtor had guaranteed an affiliate's bond obligations, for instance, or other obligations, and in that circumstance you could say perhaps that it makes sense to subordinate the claim against the debtor. That's a scenario where the affiliate language might make some sense and could be applied, but this isn't that scenario. This is not attempting to recover on the debt obligation, this is a separate obligation that they had to purchase in the ordinary course from us.

You know, I guess I would just conclude, Your Honor, with -- with the observation that you had that you would apply, following Del Biaggio, that even that it might not make sense if the words compel it, that's Congress' problem and not your problem and you're just applying the words. But not only do the words not compel it here but it just doesn't make sense.

There's no problem that would be remediated by subordinating Claren Road's claim. Claren Road is not

attempting to bootstrap itself into a higher position in the priority structure. Claren Road is really no different than any other creditor of LBI where LBI has breached an obligation. It's not altering the expectations of Claren Road that it had when it entered into the contract with LBI, it's not altering the expectations of any creditor of LBI, it has nothing to do with the capital structure or capitalization of LBI, and no one is being made worse off by allowing Claren Road's claim to be treated on a par with general creditors.

THE COURT: It occurs to me that one of the things that makes this any intriguing argument and not a plain vanilla one is that we are dealing with the circumstance that I would wager the drafters of Section 510(b) did not contemplate.

We're not dealing with a corporate debtor issuer. We're not dealing with a corporate debtor issuer's affiliate. We're dealing with a broker/dealer subject to the SIPA regime that is engaged in the ordinary course in the business of trading all kinds of securities, and it just so happens that the securities in question today are affiliate securities, bonds of LBHI.

And so the interesting question becomes, and I recognize that there is some assumptions built into what I've just said, is it sensible and consistent with the

regime for liquidating a broker/dealer for there to be a different consequence to a Claren Road type claimant when the securities that are the subject of the failed trade happened to be affiliate securities as opposed to Apple stock? That to me is the essential question. And actually none of the papers truly focused on it in quite that way.

MR. KING: Guilty as charged I suppose, Your Honor, although we did bring the Apple --

THE COURT: I know.

MR. KING: -- quote to you.

THE COURT: I appreciate it and it's a great analogy too.

MR. KING: But -- well, I didn't -- I can't take credit for it obviously.

THE COURT: I know you can't. You can take credit for quoting --

MR. KING: Yes.

THE COURT: -- from a case you like from Judge Walrath why critiquing another case you don't like from Judge Walrath.

MR. KING: I've done that to lots of judges --

THE COURT: Okay.

MR. KING: -- Your Honor. But it's not Judge Walrath who's -- who is at issue, it's the interpretation.

The -- there is no rational ground for treating it

differently, and that -- it's not -- it's not just an interesting question frankly, it is the question that is mandated by the Second Circuit in Med Diversified. Does subordinating this claim further one of those two policies underlying the statute? And it just doesn't.

I have not heard from the trustee or in the case law frankly that exists any logic for applying the statute in this circumstance, in the case of an ordinary course trade by a broker/dealer that by happenstance happens to be the bonds issued by an affiliate.

There is no reason in this circumstance, and I think that's the answer to the question and why subordination is not mandated here.

It could -- all -- there could be circumstances where those policies might be furthered. You could hypothesize somebody trying to acquire LBHI's stock and maybe there's a logic there where it's furthered. This is -- this is not that. And the Second Circuit says because the statute is ambiguous in many circumstances, because applying the plain language isn't clear, you have to look at those policies, and the policies dictate the answer, and that here is no subordination.

THE COURT: Okay.

MR. KING: Thank you, Your Honor.

MR. SALZMAN: Thank you, Your Honor. Just

briefly.

I would start with the proposition that it's not that it just so happens that Claren Road called Lehman Brothers about getting out of Lehman Brothers' bonds. If it thought there was a receptive other place to go to sell the Lehman bonds maybe it would have done that.

The affiliate provision of the statute brings directly before the Court the proposition that including in a SIPA transaction -- in a SIPA case that if you're trying to sell the securities of an affiliate back to the corporate family you should have your claim to the bonds but not your claim to also have a damages claim or have a damages claim instead.

And so I would resist the proposition that we have to assume that this was an ordinary course transaction and that it could just as easily been Apple stock. Congress --

THE COURT: But let's --

MR. SALZMAN: -- did it the other way.

THE COURT: -- let's -- let me stop you for a second and ask you this.

How significant is it to your argument that the transaction in question was an attempt by Claren Road to exist its relationship with Lehman at a time of panic in the markets?

And I ask you this question because I'm not sure

if I should be thinking about this clinically. In other words, a trade is placed, it doesn't close, the party to the trade says to the broker/dealer, you breached your obligation to me which was to complete this trade as agreed during Lehman week, presumably there were any number of -- I don't know the numbers -- but presumably there were any number of customers that were in a similar circumstance either with respect to Lehman securities or other securities.

Can you help me in this respect? I am trying to understand whether what we are dealing with here is a complete one off outlier situation in which a prime brokerage customer of the Lehman enterprise is scurrying about trying to protect its flanks at a time of market turmoil and it calls for a trade which doesn't close and it has a claim for that breach, which neither ranks as an unsecured claim in the case or is a subordinated claim, that's the binary choice. It is a claim of some sort for breach, you admit that. Yes? Absolutely.

MR. SALZMAN: That was the -- that was why it was asserted.

THE COURT: So I don't know whether or not we're talking about a class problem that affects any number of potential customers and has a meaningful economic impact in the liquidation of LBI or whether or not this is just an

intellectually interesting hypothetical which happens to have real consequences only to Claren Road.

MR. SALZMAN: To my knowledge it has consequences to Claren Road. I'm not aware of other claims in the pipeline that similarly are claims for breach of contract for LBI's failure to execute trades in Lehman securities. I'm not aware of any.

THE COURT: So this is really one off as far as you know.

MR. SALZMAN: As far as I personally know. I don't pretend to know the whole story, but I do -- I'm not aware. This came to us as Claren Road asserting this claim and we said it should be subordinated and they said, no, it shouldn't.

But I would say that the nature of their claim -- I mentioned this before -- in the LBHI case where they said we were dealing with Lehman, we don't know who -- please -- take my securities, please, that this was not a failure where Lehman -- LBI was to go into the marketplace and find a buyer, this was Lehman, at a determined price, agreeing itself -- LBI itself apparently agreeing to take the bonds at a stated price. It's not as though they had found some hypothetical buyer in the marketplace and that buyer walked away and so the trade failed, this is LBI failing to step up and buy the bonds.

THE COURT: As principal.

MR. SALZMAN: As principal. That's my knowledge. And so that presents in -- takes it out of a situation.

You might say in a SIPA case there could be a lot of people whose trades failed, a lot of peoples trades did fail during Lehman week.

This is a principal trade that LBI agreed to buy the bonds at a price certain, apparently, that's the nature of the claim being made. And so for that reason I submit it takes it out of the ordinary course or it just so happens to be situation. There could be other situations, but I submit on the record we have that's not this case.

THE COURT: Okay. Thank you.

MR. SALZMAN: Thank you.

MR. FUNKHOUSER: Rob Funkhouser from Hughes Hubbard & Reed on behalf of the SIPA Trustee, Your Honor.

In omnibus objection 104 the trustee objected to contribution indemnity claims against LBI by underwriters of LBHI securities. The claims seek reimbursement of settlements and defense costs that were incurred in securities fraud suits brought by purchasers of LBHI securities.

As set forth in the objection there were three grounds for objection, including that the claims are subject to mandatory subordination under 510(b).

There were two responses. One filed by the junior underwriters, who are 11 underwriters who collectively participated in 25 offerings of different LBHI securities in aggregate amounts in excess of $36 billion. The other was filed by UBS Financial Services who sold structured securities issued by LBHI under a distribution agreement with LBHI and LBI.

For purposes of the mandatory subordination argument UBS has adopted the position of the junior underwriters and so there's really the only -- the one opposition to consider on those issues. And from our review the Court can fully resolve both sets of claims by directing subordination under 510(b).

Based on the responses there's no disputed facts. There's a narrow issue of law that Your Honor has identified, and it applies to all claims and would obviate the need to address the other grounds for objection or other grounds that we may have reserved in the (indiscernible - 01:04:40) objection.

So like the Claren Road objection this objection addresses 510(b) subordination claims arising from the purchase or sale of LBHI securities as securities of an affiliate of the debtor.

The objection asks the Court the provide the provision of Section 510(b) that extends mandatory

subordination to reimbursement or contribution claims on account of such claims.

Based on the objection and the responses there's no dispute that the underwriters' claims are for reimbursement and contribution. There's no dispute that the claims are an account of damages claims by purchasers of LBHI securities. And there's no dispute that LBHI is an affiliate of LBI.

The narrow legal dispute for the Court is on the meaning of 510(b), and from the text of the statute 510(b) makes mandatory subordination where claims involve the securities of the affiliate of the debtor to the same extent as if the claims were securities of the debtor.

This Court has applied 510(b) to subordinate underwriter indemnity claims in Jacom Computer Services, and in doing so the Court identified that had 510(b) represents a congressional judgment that the underwriters' litigation costs, at least where it was involving debtor securities are subordinated, should not dilute the recovers on general creditor claims.

(Indiscernible - 01:06:18) relied on the Mid Diversified -- Mid-American -- Mid-American Lease Systems case from Delaware which went into more detail on the legislative history and the policies behind 510(b) as applies to reimbursement and contribution claims.

The rationale is essentially that in extending subordination to others who are involved in the process of issuing securities the risk of illegality in the issuance of securities should be borne by those who are investing in or participating in that process and not by the general creditors.

The junior underwriters don't really contest that Jacom Computer Services states the law in this district with respect to claims that are brought involving debtor securities, their narrow argument is that 510(b) does not apply by its literal terms because there's no claim or interest represented by the LBHI securities in this proceeding.

As Your Honor pointed out that is contrary to the uniform determination by other courts that have addressed the issue in the context of fraud in the purchase or sale of an affiliate securities.

We're not aware of another court having addressed it in this context of reimbursement or contribution. And the Del Biaggio court in the affirmance by the District Court of the Northern District of the California determined that the interpreting the provision of 510(b) to not apply when it was securities of the affiliate of the debtor because there weren't an interest represented by the -- by the affiliate securities would render the language

meaningless and so should be rejected as a statutory construction matter.

The argument by the junior underwriters also ignores that 510(b) requires subordination claims to claims that are senior to or equal the claim represented by the security. So it isn't necessary that there be a claim for the security in the LBI proceeding if Your Honor can identify claims that are senior to the underwriter reimbursement claims or senior to claims that would be represented by the LBHI securities.

And based on the legislative history of 510(b) and the policy that is described in the Med Diversified decision and in the courts that have applied the subordination provisions of 510(b) to underwriter reimbursement claims to DNO attempts to get reimbursement for securities liabilities it makes sense that the subordination should be to all general creditor claims.

Part of the rationale for passing 510(b) was that securities claimants wouldn't improve their position by bringing their claims as a fraud -- securities fraud claim. It makes no more sense for underwriters to be able to recover for those very same claims where they have been sued directly by the purchasers and are -- and then seek reimbursement for the same settlement from the debtor.

Under the absolute priority rule in the

(indiscernible - 01:10:12) case and principals general creditor claims are senior to securities claims regardless of whether they're direct or indirect.

It may be that there are cases where it would matter precisely where in the subordinated claims the interests of an affiliates securities would fall. It doesn't matter here because it's already clear that the general creditor claims will not be fully paid, there won't be something to subordinate.

This application of 510(b) just determining that the underwriters' claim should be subordinated to all general creditor claims would be consistent with the Court's orders on the employee equity claims that were presented in omnibus objections 101 and 131 where the trustee had asked and your order -- Your Honor directed that accrued equity award claims by employees -- and these were four LBHI securities -- should be subordinated and without determining what specific priority or amount of the claims that they would be.

If -- other Courts have taken this same course of deciding only that because the claims must be subordinated in the general creditor claims and that the general creditors will not be fully paid, it is not necessary to reach whether the claims need to be disallowed or in what amount.

The Del Biaggio case ruled that way, the Mid American Waste case from Delaware and in this district in Enron the judge also determined not to reach the other grounds for disallowance.

Your Honor, I'd be happy to answer any questions on the other grounds for disallowance of the claims that were presented in our objection and reply, but we'll rely on the papers unless there are questions.

THE COURT: But your essential argument is that the only thing I need to consider is mandatory subordination under 510(b), because for practical purposes that resolves everything. Is that right?

MR. FUNKHOUSER: That's correct.

THE COURT: Okay.

MR. BAREFOOT: Good morning, Your Honor, Luke Barefoot for the record from Cleary Gottlieb on behalf of the junior underwriters.

Your Honor, the junior underwriters I want to make clear at the outset are not making this claim in respect of their capacity as underwriters of vis-à-vis the issuer, LBHI.

Counsel for the trustee focused on many of the cases, such as Jacom and other cases which focused on the debtor's securities being underwritten.

The nature of our claim against LBI is in its

capacity as a co-underwriter of the claim. Not as an affiliate of LBHI, but in its capacity as a broker/dealer to underwrite securities, that in this case happened to be the securities of LBHI. The -- LBI also was the vast -- underwrote the vast majority both by percentage and by amount of the offerings that are at issue.

I want to focus, Your Honor, on 510(b) and on separating out what I think are two different parts of the statute, because I think in the presentations today from the trustee there was a telling disconnect.

The trustee very quickly and correctly marched through the first part of the statute, which is what types of claims are potentially subject to 510(b)?

They're correct that there's no dispute that these are claims for reimbursement of -- or contribution, that they're on account of damages for the purchase of a security, and that the security is an affiliate of the debtor. But that's not enough. You have to go to the second part of the statute which addresses to what extent claims that otherwise fit within the first half of the statute can be subordinated and to what level they can be subordinated?

I think it's also telling, Your Honor, that the trustee is not specifying to what level the claim should be subordinated, and instead is focusing on a results-oriented

outcome that says you only need to subordinate them below general creditor claims because that effectively lows to disallowance.

THE COURT: Why isn't that enough?

MR. BAREFOOT: Because that's not what 510(b) says. 510(b) does set up a very specific priority scheme that is based on the nature and priority of the security that gave rise to the claim. Those securities are bonds and preferred stock of LBHI. Those securities, as the trustee correctly conceded, and as they've gone to pains to point out in many other context, have no place in this SIPA proceeding. So there's no way to apply the literal terms of the statute that 510(b) would contemplate subordination to or below the level of those securities.

The only textual hook that the trustee attempted to offer for the first time today was that because those claims don't exist you subordinate them to zero. And the reason that doesn't work is because subordination is an inherently relative concept.

What the trustee would impose would amount to disallowance. This isn't about disallowance, this is about subordination, and you can't subordinate something to a claim that doesn't exist.

What the trustee in effect attempts to do is to create an unspecified shadow class that sits below the

general creditor claims and is entirely disconnected from the nature and the priority of the securities that the junior underwriters sold and that gave rise to the claim.

THE COURT: Let me -- let me ask you this, because I'm slightly confused as to whether or not you are responding to the argument that was made during the Claren Road phase of today's hearing or whether or not you are responding to the argument that was most recently made before you stood up.

And because you were the one who sought to have this all together as one proceeding I just want to be clear that you haven't effectively adopted that position for purposes of your own argument. Because I view this as -- we can hear whatever you want to say -- but I view this as related arguments relating to comparable issues of subordination but with different factual predicates, and I just want to be clear I'm understanding what you're telling me.

MR. BAREFOOT: Your Honor, it is different factual predicates, but those factual predicates have the exact same result where the root of the problem that Your Honor identified and that I don't want to dance around, I want to focus on, is the subordination terms relative to the security that gave rise to the claim. And the security that gave rise to the claim is a security of LBHI which doesn't

exist in this case.

THE COURT: Well is that true in a setting in which we're talking about a claim for reimbursement or contribution? And as I understand it your clients' claim is a claim against LBI as co-underwriter for damages incurred by virtue of having participated in that underwriting of these LBHI securities, correct?

MR. BAREFOOT: That's correct, Your Honor.

THE COURT: And since that is a claim that arises from the actual sale of securities and they are actually securities of an affiliate of the debtor and they are actually claims for reimbursement and contribution that in fact tie down to the sale of the securities, why does it matter for purposes of subordination? Because a literal reading of 510(b) would say you're at least below general unsecured claims, and why do we have to otherwise rank them?

MR. BAREFOOT: I disagree, Your Honor. Because the claims that we -- the securities that we underwrote that gave rise to the claim are not LBI securities.

THE COURT: I understand --

MR. BAREFOOT: They're LBHI securities.

THE COURT: -- they're in a different stack.

MR. BAREFOOT: Exactly. And if you -- if you read 510(b) it requires you to subordinate to or below the level of such security. That security, that LBHI bond has no

place in this LBI capital structure.

THE COURT: That's exactly what I was saying during the Claren Road argument in an attempt to understand how properly to scan the language of the statute, and I suggested, without having a basis for the suggestion other than I was being transparent in my thoughts, that when the affiliate language was added to 510(b) there may not have been full attention paid to how to address what occurs when we're dealing not with debtor securities but affiliate securities.

But it's nonetheless the case that the mandate of 510(b) applies to affiliate securities, and it's absolutely clear based upon the position that the claims being made here arise out of the sale of affiliate securities, and the affiliate in question is the ultimate parent of LBI, and presumably the proceeds realized from the sale of these LBHI securities funded the operation of LBI.

So under these circumstances you're making what amounts to what a certain Supreme Court justice might describe as a hyper technical argument in respect of how the statute should be interpreted that defies common sense, because the purpose here is to subordinate your very reimbursement claim, which is what the statute asks me to do and which I could easily do with putting my hammer down if I had one.

MR. BAREFOOT: Your Honor, but subordinate to where? Subordinate to the level or below the level of such security. That security isn't here.

THE COURT: So does that mean -- and let's just take this to its logical conclusion -- if we're dealing with any case involving an affiliate security we are dealing with a security that does not participate as a security of the debtor. So how do you make logical sense out of 510(b) if you assume that there is this ambiguity in it unless you apply it as it's written?

MR. BAREFOOT: Well you can't apply it as it's written because --

THE COURT: Does that mean that the statute is a nullity?

MR. BAREFOOT: No, the trustee has suggested that we're attempting to read the affiliate of the debtor language out of the statute.

THE COURT: Yes, that is what you're doing I believe.

MR. BAREFOOT: Well, Your Honor, I think that it's just that there's a more narrow universe of claims, and I think Your Honor hit it on the head of one example, which is if there were substantive consolidation, then you could -- because then the securities of LBHI would have a place in the capital structure, the cases would be together, and you

could apply the text of 510(b) to subordinate to the level of that security or below it. When those securities don't exist you can't do that. And conversely the trustee suggests that we're trying to read that portion out of the statute, but the trustee is trying to read the entire priority scheme out of the statute and suggesting that you don't have to worry about where you subordinate it to even though the statute turns on the level of the security for subordination and instead you just subordinate it to zero or to a level that's below any -- any creditor class that's in the money.

I also want to briefly address, Your Honor, the trustee suggested that the subordination is required because of this Court's prior orders on other omnibus objections. They cited to the one hundred and first and the one hundred and thirty-first omnibus claims objections. Nothing in those orders speak at all to subordination.

The trustee's objection in that -- in both of those instances moved in the alternative for the mutually exclusive remedies of either subordination or expungement and disallowance. And each of those orders is very clear that the objection is granted, to the extent set forth in the order, and that the claims are disallowed and expunged.

So there's no basis for any suggestion that Your Honor has already directed subordination of other similar

claims or that allowing these claims without subordination would somehow result in some sort of unequal treatment or inconsistency with any prior orders.

Your Honor, I also want to address -- Mr. King already addressed the disconnect in VF Brands, which just as with his claims it results in the same issue with our claims in that the Court substituted the claims of money trust for the claims of such security when money trust did not have claims against -- have securities that were issued by the debtor.

The only other textual point that I wanted to address from VF Brands is the suggestion that because the default at 510(b) is to common stock the Court could simply subordinate to the level of common stock. And that's simply inapplicable to our claims where our clients did not underwrite common stock but rather other senior classes of securities of LBHI.

So if the Court or the trustee wants to engraph the capital structure of LBHI onto LBI we may be subordinate to senior notes of LBHI, but that doesn't make it subordinate to general creditors of LBHI.

THE COURT: Well let's look at the SIPA distribution regime, which essentially -- and I may be oversimplifying it -- is customers have priority and everybody else participates as a general creditor, and

happily, for purposes of this administration, there appears to be some prospect that general creditors will receive a distribution, otherwise we wouldn't be having the argument we're having today.

So this is a very successful, perhaps the most successful in history liquidation of a major broker/dealer, and we're dealing with a very nuanced question of what the right answer should be when underwriters are seeking reimbursement from a SIPA estate in respect of alleged co-underwriter liability. And it's pretty clear that if you're going to follow the directives of 510(b) it is contemplated that claims such as the one that you're making would be subordinated to something. And what you're saying is that as a technical matter in reading this language of the statute it doesn't neatly fit and as a result you shouldn't be subordinated at all.

MR. BAREFOOT: Not pursuant to 510(b), because 510(b) sets up a specific priority scheme that simply doesn't fit the bill, and you can't -- and the other alternative, Your Honor, is that if you do want to engraph the capital structure and the priority scheme of LBHI into this LBI case the claims -- many of the securities that were underwritten were LBHI senior notes. So if we want to be junior to those that would put us into the general creditor pool at the LBHI level, not at the subordinate to the

general creditor pool.

THE COURT: But there's no authority for engrafting the capital structure of an affiliate into the debtor.

MR. BAREFOOT: There's not, and for that precise reason the fact that there is no security represented in this case to which we can be subordinated means that we cannot be subordinated if the hook for subordination is 510(b).

THE COURT: That's kind of an extreme argument. You're basically arguing impossibility that the statute as written is so hard to apply that you should get the benefit of no subordination whatsoever.

MR. BAREFOOT: I don't believe that it's an unbelievable argument, it's simply that the statute --

THE COURT: I didn't say it was unbelievable.

MR. BAREFOOT: I didn't mean to misquote --

THE COURT: I believe it. I believe you're making that argument.

MR. BAREFOOT: It's simply that the statute sets up a specific circumstance and a specific set of claims to which our claims should be subordinated. If those claims do not exist you simply can't apply the statute. It's really no different than Mr. King's argument. There may be factual differences, but the text of 510(b) applies with equal force

to both of our claims.

THE COURT: Okay. I mean I'm obviously sensitive to the issue having raised it earlier myself.

MR. BAREFOOT: Your Honor, I'll take direction, but I am prepared to address the contingency and the contractual basis for the claim. I think that there were some new arguments raised in reply on the trustee's part that I'm happy to address, to the extent Your Honor has questions or would like those addressed.

THE COURT: I frankly think that we don't need to dwell on those separate legal issues unless you feel inclined to do so, because I view the key to the current debate being rather concisely within 510(b).

MR. BAREFOOT: Very good, Your Honor.

The only final point that I would make is that there is a distinction between LBI as co-underwriter and LBHI as issuer.

If we were in the LBHI case there's no question that our claims would be subordinated and 510(b) makes very clear where they would be subordinated.

Here even though we underwrote a very small portion of the claims we suffered the lion's share of the liability compared to the 70- or 90,000 that the trustee suffered in getting the claims against it voluntarily withdrawn. And all that our claims are seeking to do is to

rectify that in a qualify through the contribution mechanism that's set forth in the master agreement among underwriters.

THE COURT: Okay. Thank you.

MR. DORCHAK: Good morning, Your Honor, Joshua Dorchak of Bingham McCutchen for UBS Financial Services, Inc.

I feel like first -- first Mr. Funkhouser didn't see fit to address the matters that I was specifically prepared to address and now it sounds like Your Honor doesn't need to hear them either, because really the main point of my presentation was going to be to focus on those issues that were specific to UBS, which has a different contract than the junior underwriters do with LBI. But I'm also willing not to take up time on issues that others don't want to take up time on.

The only thing I have to say in this case is that I support the arguments made on this side of the room on the 510(b) issue to this point. And the only thing I can add, the only thing that occurred to me while I was sitting and listening to what was a great debate was in this -- if we can agree that there's an argument in the Claren Road case that says it's just happenstance that these bonds that were the subject of the failed trade were LBHI bonds. I think there's an equally strong argument to say that the underwriters have a happenstance argument as well. We have

a -- we're suing after all not because we all invested in LBHI together, but because there's a -- the co-underwriters have liability to each other for some harm that was felt by others. It happens to be with respect to the co-underwriting of LBHI bonds, but I'm not sure that it makes any difference.

And so if we have a happenstance argument then we get to the same rational sort of step by step analysis that Your Honor was doing in the first place. Well maybe affiliates doesn't work in the last portion of section 510(b) and maybe there's a reason while it doesn't work, because maybe it shouldn't just always apply in a knee jerk way.

So again, the argument was good and I don't want to take up more of Your Honor's time unless you want to take up mine, but I did want to add that one thought.

Anything further?

THE COURT: No, that was fine.

MR. DORCHAK: Thank you.

THE COURT: Nice and brief. Is there anything more?

UNIDENTIFIED SPEAKER: Nothing further.

THE COURT: I'm going take this all under advisement, and there's a very good chance that there'll be a decision before January 31. I think there has to be a

decision before January 31. And we're adjourned, unless there's anything more.

(A chorus of thank you)

(Whereupon, these proceedings concluded at 11:36 a.m.)

C E R T I F I C A T I O N

I, Dawn South, certify that the foregoing transcript is a true and accurate record of the proceedings.

Dawn South

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